

Beyond “Plain Vanilla” Fairness Opinions

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Topics

Independent and Second Fairness Opinions

Fairness Opinions in Transactions Involving Hedge Funds

Buy-side Fairness Opinions

Firm Overview and Presenter Bio

Recent Trends in Fairness Opinions

Process, Process, Process . . .

- Financial advisors are much more involved in, and have a greater sensitivity to, “legal” process
- Special committees are more frequent and are established with a clear mandate to conduct meaningful due diligence and actively negotiate proposed transactions
- Board/Special Committee interaction with financial advisors is more frequent and better documented

Relative Fairness Receiving Greater Attention

- *Readers’ Digest*, and more recently, *Tele-Communications, Inc.* decisions in the Delaware courts
- Relative fairness questions raised in two recent transactions
 - Can a financial advisor opine as to the fairness of a transaction to “the Company” without being specific as to each class of equity?
 - In a tender offer, can a transaction be “fair” to shareholders who tender their shares but “unfair” to those shareholders who choose not, or simply fail, to, tender their shares? When can the value of the option to tender be considered?

Regulatory and Disclosure Trends

- Greater disclosure of the amount and nature of contingent fee arrangements
- Tenor of discussions regarding investment banking contingent fees has changed from “if” they are appropriate to “when” they are appropriate
- NASD proposed rule 2290 appears to have stalled – permanently?

Independent and Second Fairness Opinions

Multiple Scenarios

Financial Advisors	Fee Arrangement	Example
Two bulge-bracket investment banks, both rendering banking advice and fairness opinions	Fees for both banks are typically significantly contingent on closing of the transaction	Bain Capital, Blackstone Group acquisition of Michael's Stores (Pending)
One bulge-bracket investment bank, as "lead advisor," provides banking advice and fairness opinion. Second bulge-bracket provides only fairness opinion	Both lead advisor's fee and opinion provider's fee are typically significantly contingent on closing of the transaction	Sovereign Bancorp acquisition of Independence Community Bank (June 2006)
One bulge-bracket investment bank , as "lead advisor," provides banking advice and fairness opinion. Second independent financial advisor provides only fairness opinion	Lead advisor's fee is typically significantly contingent on closing of the transaction. Opinion provider's fee is typically non-contingent	KKR, Bain Capital, Vornado Realty Trust acquisition of Toys "R" Us (July 2005)
Investment bank/financial advisor provides financial advice and independent fairness opinion.	Fees related to advice are typically non-contingent. Fees related to opinion may or may not be contingent.	Prentice Capital acquisition of Whitehall Jewellers, Inc. (June 2006)

Independent and Second Fairness Opinions

Key Questions/Considerations

What Defines “Independence”? Ideally . . .

- Fairness opinion is provided for a previously negotiated fee and is not contingent upon the consummation of the transaction
- Advisor is engaged early enough to potentially influence deal terms and structure
- Advisor will not stand to earn fees (in addition to the fairness opinion) should the transaction be consummated

Is a Second Opinion Always Independent?

- No. A second advisor may be no more independent than the primary advisor

Are Independent Opinions a Good Idea?

- Yes. Ideally, a company receives one opinion from a competent advisor who is not providing investment banking services. Such an advisor may be in addition to an investment bank serving as lead advisor.
- However, this requires a significant change to the *status quo*. It is more realistic (at least in the short-term) to expect two opinions when a second financial advisor is retained -- one from the lead advisor and one from the second financial advisor.

Recent Independent and Second Fairness Opinions

Public Disclosure Example

Buyer:	Kohlberg Kravis Roberts, Bain Capital Partners, and Vornado Realty Trust
Target:	Toys “R” Us
Transaction Value:	\$6.7 billion
Closing Date:	July 2005

Credit Suisse First Boston delivered its opinion to the Company’s board of directors that, as of the date of its opinion and based upon and subject to the factors and assumptions set forth therein, the merger consideration of \$26.75 in cash per share, to be received by the Company’s stockholders pursuant to the merger agreement was fair from a financial point of view to the Company’s stockholders. In addition, Duff & Phelps, LLC (“Duff & Phelps”) delivered its opinion to the Company’s board of directors that, as of the date of its opinion and based upon and subject to the factors and assumptions set forth therein, the merger consideration of \$26.75 in cash per share to be received by the Company’s stockholders pursuant to the merger agreement was fair from a financial point of view to the Company’s stockholders.

The opinions of Credit Suisse First Boston and Duff & Phelps do not constitute a recommendation as to how any of our stockholders should vote with respect to the merger agreement. The full text of the written opinions of Credit Suisse First Boston, dated March 16, 2005, and Duff & Phelps, dated March 16, 2005, which set forth the matters considered and assumptions made in connection with such opinions, are attached as Annex B and Annex C, respectively, to this proxy statement. We recommend that you read each entire opinion carefully. Pursuant to the terms of the engagement letter with each of Credit Suisse First Boston and Duff & Phelps, the Company has agreed to pay to each of Credit Suisse First Boston and Duff & Phelps a fee. Substantially all of the fee of Credit Suisse First Boston is payable only upon consummation of the merger.

Source: Schedule 14A, filed with SEC May 20, 2005.

Recent Independent and Second Fairness Opinions

Public Disclosure Example

Buyer:	SuperValu, Inc.
Target:	Albertsons
Transaction Value:	\$15.5 billion
Closing Date:	June 2006

Albertsons retained three financial advisors in connection with the transactions: Goldman Sachs, Blackstone and Houlihan Lokey. Albertsons retained Goldman Sachs and Blackstone at an early stage for the purpose of, among other things, assisting Albertsons in the development and consideration of its strategic alternatives. The Albertsons board believed that retaining two internationally recognized and experienced investment banking firms for this purpose would provide greater assurance of a thorough process than the retention of a single firm. The terms of the engagements of Goldman Sachs and Blackstone provided, among other things, that if requested by the Albertsons board, Goldman Sachs and Blackstone would provide opinions regarding the fairness, from a financial point of view, of the consideration to be received by Albertsons stockholders in specified types of transactions involving the sale of 50% or more of the stock or assets of Albertsons. Subsequently, Albertsons retained Houlihan Lokey for the limited purposes of providing solvency advice and to provide an opinion regarding the fairness, from a financial point of view, of the consideration to be received by New Albertsons stockholders in the Supervalu merger. Unlike the arrangements with Goldman Sachs and Blackstone, the arrangements with Houlihan Lokey did not provide for any fee that was contingent on the completion of any transaction. Albertsons and its board of directors believed that the participation of Houlihan Lokey in the process would provide an additional source of advice to the board.

Source: Company S-4/A, filed with SEC April 18, 2006.

General Hedge Fund M&A Trends

- It's not just Cerebus and GMAC -- hedge funds have moved aggressively into the middle market
- Increasing trend to larger equity positions, more active management and longer investment horizons
- Hedge funds often invest in companies operating under some degree of financial strain
- Many hedge funds are prepared to invest in all levels of the capital structure (esp. for middle market) and will frequently propose (or facilitate) a significant recapitalization of the target
- Many middle market companies have difficulty responding, in an agile fashion, to hedge fund shareholder activism

Fairness Opinions in Hedge Fund Transactions

Key Questions/Considerations

As a company approaches the zone of insolvency, a fairness opinion may have significant limitations

- Fairness opinions address fairness to shareholders (only)
- A solvency opinion may be required in lieu of, or in addition to, a fairness opinion
- In some instances, a better alternative may be a contractually-defined financial opinion that collectively considers the interests of shareholders, the company, lenders, vendors, and other creditors.

What is the value of avoiding bankruptcy? For common equity, is ANY non-bankruptcy alternative fair?

- Duff & Phelps recently reviewed a contemplated PIPES transaction in which the infusion of equity may have forestalled a bankruptcy filing but the contemplated offering price was at a substantial discount to the fair market value of the equity

Consideration in hedge fund transactions often entails non-traditional valuation approaches

- Bridge loan
 - Convertible debt
 - Warrants
 - Critically-needed working capital infusion
- May, in part, replace senior credit

The financial advisor must determine if it is appropriate for the fairness opinion to take into account “non-traditional” factors?

- Break-up fees
- Commitment/funding/management fees
- Time required to close
- Certainty of closing
- Receptivity of senior creditors/key vendors/key customers?

Recent Opinions in Hedge Fund Transaction

Public Disclosure Excerpts

Buyer:	Prentice Capital Management
Target:	Whitehall Jewellers, Inc.
Transaction Value:	\$27.2 million
Closing Date:	June 2006

On April 19, 2005, Newcastle Partners, L.P., an investment fund, and various related persons (collectively, the “Newcastle Parties”) filed a Schedule 13D indicating that they owned 2,018,400 Common Shares as of April 15, 2005, then representing 14.5% of the Company’s outstanding Common Shares.

On June 23, 2005, the Company announced the election of Mr. Steven J. Pully, the President of Newcastle Management, L.P. (“Newcastle”), as a director.

On July 12, 2005, the Board of Directors formed a special committee . . . to consider potential financing proposals in light of Newcastle’s interest in being a potential source of financing and Mr. Pully’s status as Chairman of the Board.

The [September 21, 2005 proposal] from [Prentice Capital Management L.P.] contemplated a term sheet, which the Company signed on September 21, 2005. . . . The Prentice Term Sheet was nonbinding, except that the Company was required to deal exclusively with Prentice through September 24, 2005 (which was subsequently extended).

[On] October 3, 2005. Representatives of Duff & Phelps verbally presented their views of the fairness of the Prentice proposal. They reviewed various analyses and opined that, as of the date of their opinion, the terms of the Prentice proposal were fair to the stockholders of Whitehall from a financial point of view.

On January 23, 2006, the Board of Directors was advised by Duff & Phelps that the Newcastle transaction would constitute a “Superior Proposal,” which was defined under the Securities Purchase Agreement as a transaction that was both more favorable from a financial point of view to the Company, its stockholders and creditors, taken as a whole, than the terms of the Securities Purchase Agreement and also reasonably capable of being consummated.

Duff & Phelps delivered its oral opinions that the proposed [revised] Prentice transaction was fair to the stockholders of the Company, other than the Investors or their respective affiliates, from a financial point of view, without giving effect to any impacts of the proposed transaction on any particular stockholder other than in its capacity as a stockholder, and that the revised Prentice transaction was more favorable, from a financial point of view, to the Company, its stockholders and creditors, taken as a whole, than the Newcastle binding proposal. The Board of Directors concluded that the January 24 Newcastle binding proposal no longer constituted a “Superior Proposal” (as defined in the Securities Purchase Agreement) relative to the revised Prentice transaction.

Buy-Side Fairness Opinions

Most fairness opinions consider the “fairness” of a contemplated transaction to the Target’s shareholders

- Asks: Are the Target shareholders receiving “enough”?

A “buy-side” opinion considers the “fairness” of a contemplated transaction to the Acquirer's shareholders

- Asks: Are the Acquirer shareholders paying “too much”?

Buy-Side Fairness Opinions

Typical Scenarios

Transaction value depends meaningfully on the realization of expected synergies

- A transaction value that is “fair” only if 100% of the synergies are realized may be difficult to justify
- It is often useful for a Board of Directors to understand the extent to which the synergies must be realized in order for the value to be “fair”
- This is particularly relevant if the Target represents a significant growth platform for the Acquirer

The economic value of the Target is significantly dependent on the Acquirer

- Vertical dependence, e.g., Acquirer is Target’s largest customer or vendor
- Target receives significant financing from Acquirer
- Key Question: What is the stand-alone value of the Target? Is the Acquirer paying for the benefit it provides?

Acquirer and Target have common large shareholder(s)

- Such a shareholder may be less sensitive to “paying too much” if the consideration simply represents a transfer of value from one investment position to another

In the case of a stock transaction, the value of the Acquirer shares may not be accurately captured by an exchange traded price

- Thinly-traded stock and/or a small public float
- Stock price under short-term pressure
- May need to adjust exchange traded price to account for Acquirer ownership in equity of another company
- Material non-public information may result in an exchange traded price that under-values the Acquirer (e.g., large new contract, pending FDA approval, etc.)

Specified Purpose Acquisition Company (“SPAC”)

- Acquisition funds often subject to “use it or lose it” provisions

Recent Buy-Side Opinions

Buyer: Boulder Specialty Brands, Inc. (publicly-traded SPAC)
Target: GFA Brands, Inc. (Smart Balance® and Earth Balance®)
Transaction Value: \$465 million
Closing Date: *Transaction Pending*

In connection with the proposed transaction, Duff & Phelps, LLC provided a fairness opinion to the Board of Directors of Boulder. . . . Citigroup Global Markets, Inc. was an advisor to Boulder, and Davis & Kuelthau s.c., Ellenoff Grossman & Schole LLP and Foley & Lardner LLP were Boulder's legal advisors.

Source: Company DEFA14A, filed with SEC September 27, 2006.

Buyer: Magellan Health Services, Inc. (public)
Target: National Imaging Associates, Inc. (private)
Transaction Value: \$122 million (cash)
Closing Date: December 2005

Fairness opinion not publicly disclosed

Buyer: Akamai Technologies, Inc. (public)
Target: Speedera Networks, Inc. (private)
Transaction Value: \$167.6 million
Closing Date: June 2005

Fairness opinion not publicly disclosed

Duff & Phelps Overview

Fairness & Solvency Opinions

M&A Advisory

ESOP & ERISA Advisory

Financial Reporting Valuation

Tax Valuation & Consulting

Real Estate & Fixed Asset Services

**Dispute Consulting &
Forensic Advisory Services**

Duff & Phelps is one of the world's leading independent financial advisory firms serving client needs in the areas of valuation, investment banking and transaction advice, and dispute consulting. We are the foremost provider of industry focused, independent and objective valuation insight and advice. Our services include financial reporting and tax valuation, transfer pricing, real estate and fixed asset services, merger and acquisition advisory, fairness and solvency opinions, due diligence and dispute consulting.

Our professionals bring practical experience, responsiveness and a collaborative approach to satisfy our clients' needs with the rigor and independence that the market demands. When our clients can't afford to get their analysis wrong, they look to Duff & Phelps to get it right.

With more than 700 employees serving clients worldwide through offices in the United States, Europe and Asia, Duff & Phelps is committed to delivering insightful advice and service of exceptional quality, integrity and objectivity.

If you would like to learn more about Duff & Phelps, visit our Web site at www.duffandphelps.com or call us directly at +1-866-282-8258.

Professional Credentials



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Yvette R. Austin Smith is a Director in the New York office of Duff & Phelps, LLC and a member of the firm's Investment Banking and Transaction Advisory Services practice. Ms. Austin Smith regularly provides financial advisory services and financial opinions for M&A and financing transactions. In addition, she has frequently served as a consulting expert in litigation matters involving M&A, securities fraud and bankruptcy. Ms Austin Smith is frequent speaker and author on topics related to valuation and M&A.

Professional Experience:

- Ms. Austin Smith advises clients on a wide-range of transaction-related issues including fairness opinions, solvency analysis/opinions, valuation of illiquid financial securities and related party financing.
- Yvette focuses on the middle-market and has advised on transactions in the retail/consumer products, healthcare and entertainment industries, for both public and private companies.
- Advised transactions include cash and stock mergers and acquisitions, going-private transactions, friendly and hostile tender offers, LBOs, PIPES and equity rights offerings.
- She is currently providing valuation commentary to a forthcoming revision of the American Bar Association Model Public Company Acquisition Agreement. She is also a contributing editor for a forthcoming ABA Dictionary of M&A Terms. Additionally, Ms. Austin Smith is a member of the National Association of Corporate Directors.
- Recent clients include Louis Vuitton Moët Hennessy, Sanofi-Aventis S.A, Whitehall Jewellers, Inc., Magellan Health Services, Inc., and ROW Entertainment Income Fund (now: Entertainment One)
- Prior to joining D&P, Yvette was a core member of Ernst & Young's Strategic Finance and Securities, M&A and Ownership Disputes practice areas

Education & Certifications:

- A.B. - Harvard University
- M.B.A. - Columbia Business School
- Substantial graduate coursework in applied financial mathematics - New York University's Courant Institute of Mathematics

Professional Associations & Affiliations:

- American Bar Association, Associate Member
- National Association of Corporate Directors, Member